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SUPPORTING BUYER-SUPPLIER RELATIONSHIPS

TECHNICAL BRIEF NO. 1



July 2007

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Weidemann Associates, Inc.

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Business Growth Initiative

Technical Brief

Supporting Buyer-Supplier Relationships

Market linkages are a popular intervention for enterprise development practitioners. As communication channels extend, accessibility to market information expands, and regional and international trade channels open, it is becoming easier to link local suppliers in lower income countries to international buyers and markets. Yet, facilitating the connection between suppliers and buyers is not enough to ensure that profitable relationships occur, much less endure. Making these relationships last requires open communication, a clear articulation of each party's expectations and incentives, and a mutual understanding of capabilities, responsibilities, and standards. Without these factors, donors may be successful in bringing buyers and suppliers together for initial orders, but the relationships fail to produce long-term business transactions in situations where buyers can pass on increasingly high value activities and responsibilities to their suppliers.

Points to consider in strengthening and monitoring buyer-supplier relationships

Buyer-supplier relationships can be analyzed from three perspectives: the buyers, the suppliers, and facilitating governments and donors. There are a number of key questions for each party that should be considered.

Through six case studies, a recently completed USAID study sought to understand in more depth the success factors in cultivating and sustaining export opportunities in under-developed countries, particularly the activities and approaches necessary to create sustainable buyer-supplier relationships. This brief includes key questions on the topic of sustainable buyer-supplier relationships, the framework around which the case studies were considered, lessons learned and recommended steps for donors in facilitating market linkages and buyer-supplier relationships. The six case studies are summarized at the end of this brief.

For International buyers:

- What distinguishes the suppliers that successfully deliver with those that fail?
- What do buyers look for to assure them that suppliers will be able to deliver on an order?
- What types of support mechanisms are used by buyers to ensure that the suppliers deliver on the orders?

For suppliers:

- What are the key issues that need to be managed to satisfy the quality and quantity requirements for an international order?
- What else do suppliers need to manage, outside of the product specifications and timing of the order?
- How can a one-time order be parlayed into a long-term relationship?
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For governments and donors:

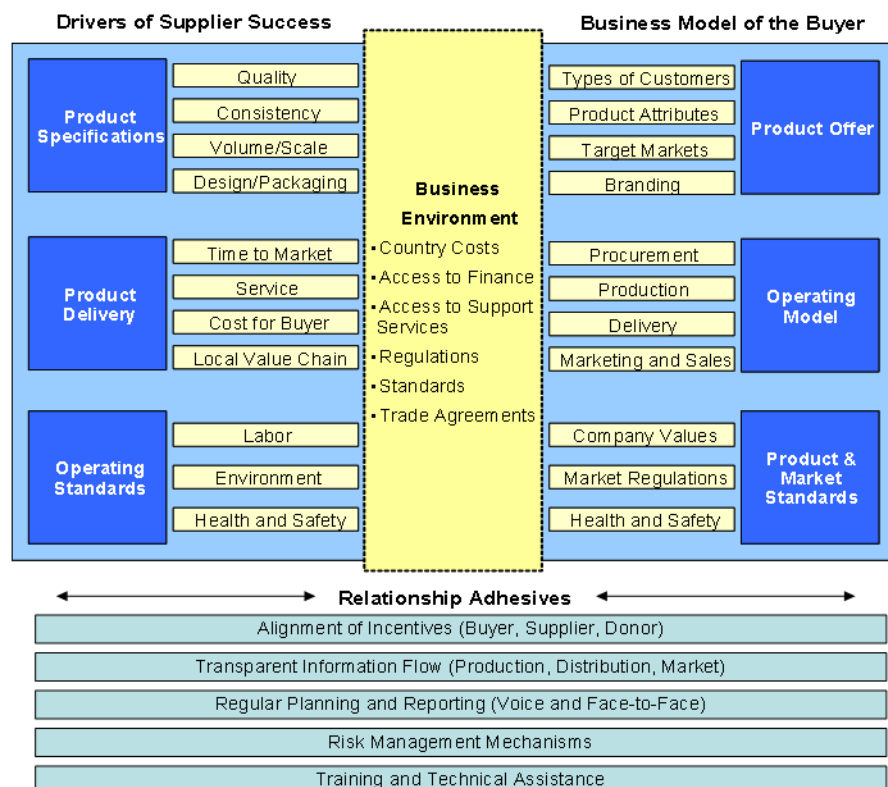
- What are the constructive roles that a government/donor can play in supporting export promotion at the firm and industry level?
- What strategies/support mechanisms have been used successfully to assist a firm in transforming the first contract into a sustainable relationship?
- How should the donor or government plan its exit strategy?

The Buyer-Supplier Relationship Framework

Figure 1 represents the buyer-supplier relationship framework. The framework is structured around three dimensions: 1.) the market and management parameters that determine the buyer's business model; 2.) the dimensions along which suppliers deliver value to their buyers; and 3.) the business environment conditions within which the relationship takes place. The closer the supplier can come to delivering value along each of the dimensions below – product specifications, product delivery, and operating standards – the more likely the relationship will be seen as successful by the buyer.

However, a supplier can successfully deliver the necessary value one year and then fail the next. Market needs can and do shift, product specifications change, and time to market shrinks. The lifecycle of a commercial relationship can be characterized by five stages:

Figure 1: Buyer-Supplier Relationship



Source: JE Austin Associates, 2007

1. Upfront investment in the product and the relationship by both parties
Assumption of transactional risk and mitigation of risk
2. Creation and delivery of (product) value
3. Increase in the number of transactions (assuming success in the marketplace)
4. Responses to shifts in the market

After the first transaction, the supplier continually faces the challenge of keeping up with the buyer and its end-market.

The ability of the supplier to stay on top of the shifting needs of the buyer is largely determined by “relationship adhesives.” Relationship adhesives essentially provide glue to the relationship thereby increasing the probability that the supplier is aligned with, and can adapt to, the needs of the buyer over time.

Lessons Learned

Product specifications will get the supplier in the door, but an alignment with the buyer's business model will get an invitation to stay.

The demonstrated ability of a supplier to meet product specifications at a competitive cost is enough to create a market linkage, but the sustainability of the buyer-supplier relationship requires more than just delivering a product at a given price. From the buyer's perspective, if a procurement decision is only based on cost, then as new supply options emerge, there will frequently be a cheaper supplier producing equal or better quality. To maintain its competitiveness, the supplier needs a full understanding of the buyer's business model, a comprehensive set of competencies to serve that business model, and favorable conditions in the business environment.

“Relationship adhesives” increase the probability that the supplier is aligned with, and can adapt to, the needs of the buyer over time. Donors have a role to play in ensuring that the adhesives are in place and functioning well. As mentioned above, the supplier continually faces the challenge of keeping up with the buyer and its end-market.

The ability of the supplier to stay on top of the shifting needs of the buyer is largely determined by “relationship adhesives.” The specific adhesives highlighted and discussed in more detail in the report include:

- Understanding and alignment of incentives for all parties, including the donors,
- Transparent, continuous information flow on market needs/production requirements,
- Regular planning and reporting throughout the production, marketing and sales cycle,
- Risk management mechanisms to ensure that both the supplier and the buyer are effectively mitigated against any commercial risk and
- Training/technical assistance to ensure the highest quality and production standards.

Aligning incentives among buyer, supplier and facilitator is particularly critical to making a relationship endure. Facilitators (donors and governments) can play an important role in linking suppliers with buyers, coordinating technical assistance to increase supplier capacity, and exposing the supplier to dynamic market needs. However, it is also important for facilitators to weigh and understand the incentives that drive the relationships for all parties, including the incentives for the facilitators themselves.

When standards matter, continuously seek a third opinion. For relationships that require high quality and social responsibility standards, a third party who monitors the production and provide ongoing quality control based on specific, transparent criteria can be instrumental in keeping the supplier aligned with the buyer needs.

Understand the risks of relying on a cottage industry, or group of informal micro-enterprises, to serve an international market. For a supplier, subcontracting production with informal micro-enterprises can provide a low cost solution for basic production, but it also can

expose the buyer and the entire value chain to compromised quality and labor standards. Sustainable relationships require that these risks be fully understood and carefully managed.

Successful relationships take time to establish and develop – donors have a role to play, both in making the linkage and in setting expectations. Buyers unfamiliar with a specific production and general business environment can underestimate how long a relationship can take to develop. Donors and governments can play a role both in setting realistic expectations and in building trust between the parties in the early stages of the relationship.

Donors Acting as Market Facilitators: Turning Lessons into Action

Whether they are working with suppliers of large scale retailers or boutiques, donors have a role to play in ensuring that the relationship adhesives in Figure 1 are in place and functioning well. However, not all facilitation is good. If designed in the wrong way, a donor-driven market linkage can result in donor dependence or worse in a distortion in the market and an inefficient misallocation of scarce investment resources. The six cases highlight a number of design principles for donors that are considering a market linkage intervention:

1. **Understand and align incentives among the buyer, supplier and facilitator.** Buyers often do not understand the production capacities and business environment of a particular country and so structure orders and contracts that are not aligned with local conditions. Similarly, suppliers rarely understand the end-market needs and trends for their products and so are not fully aware of the buyer's business model. The donor, as a facilitator, is uniquely positioned to bridge this gap.
2. **Foster a buyer-supplier relationship in which the buyer is transferring end-market information directly to the supplier on a regular basis.** Buyers often fail to communicate end market needs back to their suppliers and deal with their suppliers on a "need to know" basis. Again,

the donor is well-positioned to foster a more open relationship.

3. **Support open, transparent and regular planning/reporting between the buyer and supplier.** Suppliers can be too ambitious in their production promises. Regular reporting is critical to building and preserving trust with international buyers.
4. **Build the capacity of the supplier in customer relationship management (CRM) skills.** Current market linkage projects invest in production upgrading and creating the initial linkage but stop short of providing extended support in learning how to manage the relationship. CRM tools and techniques can be instrumental in ensuring a supplier is able to stay connected to its buyer over time.
5. **Establish clear and transparent criteria and support third party quality control and certification agents** in sectors that require high quality and social responsibility standards.
6. **Support suppliers in understanding the risk/reward** associated with different market penetration strategies
7. **Know the exit strategy before intervening.** When designing a market linkage intervention, the following three questions can ensure that the appropriate exit strategy is adopted:
 - Does the market provide incentives for either party (supplier or buyer) to take over the market linkage or facilitation activities over time?
 - If neither party is likely to play the role of the facilitator, then is there a market for an independent third party to provide sustainable fee based services?
 - If there is no market for fee-based services, then is there a credible rationale for subsidizing the market (e.g., market failure)?

The Cases

Brazil Uruku Pigment: Aveda and the Yawanawa tribe

In Brazil, an indigenous tribe produces a pigment used by an international cosmetics company for its specialty product line. The relationship enabled the tribe to become economically independent and supplied the cosmetics company with a unique natural and organic product, but was heavily reliant on an unusual type of facilitator to solidify the buyer-supplier relationship. This case tracks the relationship between the Brazilian Yawanawa tribe that produces uruku pigment, and the



The Yawanawa tribe of Brazil continues to supply US cosmetics producer Aveda with a unique natural and organic product for a specialty line of cosmetics.

United States-based personal care product and cosmetics company, Aveda Corporation. This international buyer-supplier relationship has enabled the Yawanawa tribe to become economically independent and has supplied Aveda with a unique natural and organic product for a specialty line of cosmetics. This case demonstrates the role of the market and non-market facilitators. In addition, the case highlights the importance of intermediaries and third-party quality control over local harvesting and production bound for high-end markets.

Tanzania Coffee: Peet's and Kilimanjaro

This case tracks the relationship between Tanzanian coffee farmers in the KILICAFE

cooperative, the International NGO TechnoServe (through funding from USAID, USDA and Switzerland's Secretariat for Economic Affairs), and the United States-based specialty coffee company Peet's Coffee & Tea. This international buyer-supplier relationship represented the first direct export of Tanzanian coffee after tax and export policies regarding coffee were changed by the Ministries of Agriculture and Finance to create a more globally competitive coffee industry. This case demonstrates the role that a non-market facilitator can play in supporting both the production and policy aspects to a relationship. The facilitator, Technoserve, enhanced the supplier's ability to meet and maintain high product quality, as well as worked with the government to encourage and create an enabling environment for long-run success. This case also demonstrates the importance of having a supplier maintain flexibility in delivering on quantity agreements over time.

Ghana Apparel: Wal-Mart and Belin Textiles

In Ghana, a textile manufacturer took advantage of duty-free zones and preferential trade agreements to export low-margin, low-cost garments to US buyers but required innovative product designs and product differentiation to establish repeat orders. This case tracks the relationship between a Ghanaian textile manufacturer (Belin Textiles) and end buyers in the United States. The case will highlight the benefits that suppliers potentially experience when taking advantage of preferential trade agreements for duty-free exporting. The case will also demonstrate that locating in duty-free zones is not enough to win business; suppliers must market themselves in the venues where their buyers seek them, like well known trade shows. Finally, the case will show that by continually innovating product design, and differentiating their products, suppliers have better chances for repeat orders and the possibility for longer-term supplier relationships.

Ghana Handicrafts: Target, MarMaxx, Pier 1, and Tekura Enterprises

In Ghana, a Ghanaian entrepreneur with local production expertise, a tested product portfolio, and a network of international buyers develops relationships with a number of big-box retailers. This case tracks the relationship between Ghanaian handicraft manufacturers, (Tekura Enterprise Ltd, and others) and end buyers (Pier One, MarMaxx, and Target) in the United States. The case will highlight the benefits and risks suppliers can experience when doing business with big box retailers. The case reveals the importance of the supplier's ability to access timely end-market information in order to track changes in customer preferences and anticipate changes in the buyers' needs. In addition, this case explores the importance of pre-emptive and continual innovation of product design in order to mitigate the risk replication (copy-cat competition), help protect margins, and build demand in new markets.



Tekura artisan finishing a wooden vase

Pakistan Sporting Goods Equipment: Nike and Saga Sports

In Pakistan, a sporting goods manufacturer supplied soccer balls for a global sporting goods company through a cottage-industry manufacturing model. However, the model ultimately left the supplier and its buyer vulnerable to violations of international labor standards. This case outlines the relationship between a Pakistan sporting goods manufacturer, Saga Sports, and Nike. The case illustrates how doing business with international brands requires an integration of processes and

full adoption of international standards. Specifically, the case will explore the importance of institutionalized processes within the supplier and the need for the supplier to internalize the brand equity of its buyer and uphold end-market standards. The case will explore the difficulties of monitoring and enforcing production standards in cottage industries.

Rwanda Coffee: Starbucks and Local Producers

Prior to 2001, Rwanda was an unknown in the specialty/high-value coffee sector. Today, Rwanda is a sought-after market supplying specialty coffee to Starbucks and other premium coffee buyers throughout Europe and the United States. The transformation is due to the combined efforts of the local producers, the Government of Rwanda, USAID donor projects, and international buyers. This case focuses on the role of the USAID donor projects in upgrading the quality of supply and then facilitating the initial linkage with international buyers. The case illustrates best-practice training and facilitation in preparing a product to meet international quality standards and attracting the interest of international buyers. Finally, the case highlights the continuing need to build the capacity of local suppliers in marketing and commercial relationship management.



Rwanda, who now supplies coffee for Starbucks' Blue Bourbon brand is one of a select group of Starbucks' Black Apron Exclusives line of world class specialty coffees.

U.S. Agency for International Development

1300 Pennsylvania Avenue, NW

Washington, DC 20523

Tel: (202) 712-0000

Fax: (202) 216-3524

www.usaid.gov